

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Smyth, et al. Analyst: Matthew Cooling Bill Number: AB 233
Related Bills: See Legislative History Telephone: 845-5983 Amended Date: May 26, 2009
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Pet Adoption Costs Deduction/Pet Adoption Costs Deduction Fund

SUMMARY

This bill would allow taxpayers a miscellaneous itemized deduction, up to \$100 per taxable year, for the qualified costs paid or incurred during the taxable year for the adoption of pets from a qualified animal rescue organization and would establish the Pet Adoption Cost Deduction Fund.

SUMMARY OF AMENDMENTS

The bill as amended May 26, 2009, would add two provisions related to the proposed Pet Adoption Cost Deduction.

Provision 1 would provide an annual \$1 million allocation limit to the Pet Adoption Cost Deduction. Provision 2 would establish a voluntary contribution fund (VCF) designation to reimburse the General Fund for the revenue losses associated with the Pet Adoption Cost Deduction and would allow any funds collected from the VCF in excess of the amounts necessary to fund the Pet Adoption Cost Deduction to be distributed to municipal shelters, as specified.

As a result of these amendments, the department's analyses of the bill as amended April 13, 2009, and May 4, 2009, no longer apply.

SUMMARY OF SUGGESTED AMENDMENTS

Amendment 1 is provided to suggest appropriation language to fund the department's costs to implement this bill.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to encourage pet adoptions, thus relieving the overpopulation of animals in shelters.

Board Position:	Department Director	Date
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_____ N _____ OUA _____ X PENDING	Selvi Stanislaus	06/04/09

EFFECTIVE/OPERATIVE DATE

Assuming enactment in 2009, this bill would be effective January 1, 2010. Provision 1 of this bill would be specifically operative for taxable years beginning on or after January 1, 2010, and before January 1, 2015. Provision 2 would be operative as of January 1, 2010, and would apply to returns filed on or after that date.

POSITION

Pending.

SUMMARY OF REVENUE IMPACT

Estimated Revenue Impact of AB 233 Effective For Taxable Years Beginning On Or After January 1, 2010, And Before January 1, 2015 Enactment Assumed After June 30, 2009				
	2009-10	2010-11	2011-12	2012-13
Provision 1: Pet Adoption Deduction Costs	-\$2,000	-\$50,000	-\$50,000	-\$60,000
Provision 2: Pet Adoption Cost Deduction Fund	NA	-\$15,000	-\$15,000	-\$15,000
Net General Fund Impact¹	-\$2,000	-\$65,000	-\$65,000	-\$75,000

ANALYSIS

Provision 1

FEDERAL/STATE LAW

Existing federal and state laws allow individuals to deduct from their adjusted gross income (AGI)² either a fixed amount (indexed for inflation), known as the standard deduction, or the amount of a taxpayer's itemized deductions, whichever is greater. Certain expenses, such as medical expenses, charitable contributions, interest, and taxes, are deductible as itemized deductions.

Currently, there is no federal or state law that provides a tax benefit for adopting a pet from an animal shelter or nonprofit animal welfare organization.

¹ Because of the uncertainty for the timing of the reimbursement to the General Fund, this summary does not include General Fund reimbursement from the VCF designation.

²For purposes of state income tax law, AGI is defined by cross-reference to the Internal Revenue Code (IRC) as gross income, which includes all income from whatever source derived, adjusted for certain allowable amounts, including IRA contributions, alimony paid, moving expenses, and Keogh account contributions.

THIS PROVISION

Under the Personal Income Tax Law (PITL), this provision would allow a taxpayer to deduct the expenses paid or incurred to adopt an animal from a qualified animal rescue organization as a miscellaneous itemized deduction not subject to the 2 percent of AGI limitation.

This provision would define a “pet” as any animal adopted from a qualified animal rescue organization that is not used for the production of income or in a taxpayer’s trade or business. This provision would also clarify that a “qualified animal rescue organization” would mean a public animal control agency or shelter, a humane society shelter, or rescue group.

For purposes of this provision, a rescue group would be a non-profit group under Internal Revenue Code (IRC) section 501(c)(3) whose primary purpose is to rescue and place dogs, cats, or other animals removed from a public animal control agency or shelter or that have been surrendered or relinquished by a previous owner.

The maximum deduction per eligible taxpayer allowed by this provision would be \$100 for each taxable year, beginning on or after January 1, 2010, and before January 1, 2015. This provision would also limit the deduction to \$100 per pet adoption. This provision would allow a taxpayer who adopts two pets in one year to deduct the fees paid or incurred, in excess of \$100, in the following years. This deduction would be subject to an overall \$1 million annual limitation.

This provision would require eligible taxpayers to claim this deduction on their timely-filed original personal income tax returns. The Franchise Tax Board (FTB) would be required to monitor the returns filed and periodically provide information on its Web site related to the amount of deductions claimed on returns. When FTB estimates that the \$1 million limit will be reached, a cut-off date would be established and published on FTB’s Web site. The cut-off date would be the last day of the calendar quarter in which FTB estimates the \$1 million limitation would be reached. After the cut-off date, FTB would begin to deny all deductions on income tax returns received after that date and notify the taxpayers that their deduction would be denied. Any disallowance would be treated as a mathematical error; any additional tax would be assessed and collected by FTB.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concern. Department staff is available to work with the author’s office to resolve this and other concerns that may be identified.

Under this provision, FTB would accept all deductions reported on or before the cutoff date regardless of the \$1 million allocation cap. As a result, FTB would be unable to ensure that the deduction does not exceed the maximum amount provided for under this provision, which would result in a greater than anticipated revenue impact.

FISCAL IMPACT

This provision would require an additional line to be added to the personal income tax return and entered into the taxpayer information system. As a result, this provision would impact the department’s processing, costs for tax returns, costs for systems programming, and the monitoring of this deduction.

The costs to implement this provision are estimated to be approximately \$736,000, which includes 10 P.Y.s in the first year and approximately \$525,000 in each additional year in which this deduction would be allowed. Amendments 1 through 3 have been provided to request an appropriation for the department's costs to implement this bill. Lack of an appropriation would delay funding to implement this bill until June, 2010, delaying implementation until taxable years beginning on or after January 1, 2011.

ECONOMIC IMPACT

Revenue Estimate

Because of the uncertainty for the timing of the reimbursement to the General Fund, this provision could result in the following revenue losses:

Estimated Revenue Impact of AB 233 Pet Adoption Fee Deduction Effective For Taxable Years Beginning On or After January 1, 2010, and Before January 1, 2015 Enactment Assumed After June 30, 2009					
2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
-\$2,000	-\$50,000	-\$50,000	-\$60,000	-\$60,000	-\$30,000

Revenue Discussion

The revenue impact of this provision would depend on the number of qualifying taxpayers who adopt a cat, dog, or other animal that has been removed from a qualified animal rescue organization; claim itemized deductions, not subject to the 2 percent of adjusted gross income limitation, on their tax returns; and derive a deduction benefit from pet adoption costs. This estimate does not include General Fund reimbursement from the VCF designation.

For purposes of this analysis, only cats and dogs were included as pets. Though there are numerous resources for those wishing to adopt a pet, little reliable data on the number of pet adoptions is available. This estimate assumes that the deduction would be claimed in the taxable year in which the expenses are paid or incurred.

California specific data from the National Animal Interest Alliance indicate that approximately 68,000 cats and 100,000 dogs from shelters were placed in homes in 2007. The total of 168,000 cats and dogs was doubled to include pets adopted from qualifying IRC section 501(c)(3) organizations for a 2007 figure of 336,000 pets (168,000 X 2). Data from the American Veterinary Medical Association gives an annual pet growth rate of approximately 1 percent. The 336,000 figure for pets would grow to approximately 345,000 by 2010.

Tax return data indicate approximately 4.4 million taxpayers report itemized deductions and derive a deduction benefit. Assuming 5 percent of these taxpayers, or approximately 220,000 (4.4 million taxpayers X 5%), would adopt a pet, deductible adoption costs would be approximately \$22 million (220,000 taxpayers X \$100 deduction limit). However, the deduction would be limited to \$1 million. Applying a marginal tax rate of 6.25 percent would result in an annual revenue loss of \$62,500 for 2010 (\$1 million X 6.25%). Beginning with 2011, the marginal tax rate is 6 percent, and results in a revenue loss of \$60,000.

Because this would be a new deduction, a learning curve would be applied to the rate at which taxpayers would claim the deduction. The assumed rate would be 60 percent in 2010, increasing to 95 percent in 2013. In 2010, the impact would be \$37,500 (\$62,500 X 60%). By 2013, the impact would be approximately \$58,700 (\$61,800 X 95%).

Provision 2

FEDERAL/STATE LAW

Current federal tax law provides a checkoff to direct \$3 of a taxpayer's tax liability to the presidential election fund. Designation of the \$3 amount does not affect a taxpayer's tax liability or refund amount.

Current state tax law allows taxpayers to make contributions of their own funds (not tax liability) on their personal income tax returns to the 15 VCFs listed on the state tax return. Each fund provides for the reimbursement of FTB's and the Controller's actual costs to administer the fund.

Except for the California Seniors Special Fund, which has no sunset date, the voluntary contribution funds have various sunset dates. The initial minimum contribution amount is \$250,000, which is indexed annually for each fund.

Current state law provides that if the number of contingent voluntary contribution designations³ that are eligible to be added to the return is greater than the number of designations removed, then the voluntary contribution designations will be queued and added to the return in order of the date of enactment.

THIS PROVISION

This provision would establish the Pet Adoption Cost Deduction Fund and would allow taxpayers to designate their own funds (not tax liability) for contribution to the fund on their personal income tax returns in full dollar amounts of \$1 or more. Each signatory on a joint return may make the contributions individually. The designations for any taxable year must be made on the initial return for the taxable year and, once made, are irrevocable.

This provision would require FTB to revise the personal income tax return to include a designation space for the fund beginning with the first taxable year another VCF is removed.

For the second taxable year the fund is on the return, this provision would require the fund to meet the \$250,000 minimum contribution test. FTB is required to estimate by September 1 of any calendar year after the first taxable year the fund appears on tax returns that contributions made under this provision will be less than \$250,000 (as indexed for inflation). The law authorizing designations for this fund would be repealed if contributions made under this provision will be less than the minimum contribution amount.

³ A contingent voluntary contribution designation is a voluntary contribution designation that contains specific language stating that it may not be added to the return until another voluntary contribution designation is removed from the return.

This provision would allow the voluntary contribution designation to remain on the tax return for five years unless a later enacted statute deletes or extends that date.

Beginning with the third calendar year after the fund appears on the personal income tax return, FTB would adjust the minimum contribution amount for the fund by September 1, of that year. The minimum contribution amount would adjust according to the California Consumer Price Index (CCPI), as specified.

This provision would specify that if payments and credits reported on the return do not exceed the taxpayer's liability, then the taxpayer's return shall be treated as if no designation has been made. If no designee is specified, a designated contribution amount would be transferred to the General Fund.

This provision would require all money transferred to the Pet Adoption Cost Deduction Fund to be allocated, upon appropriation by the Legislature, to the State Controller to reimburse the General Fund for the loss associated with the Pet Adoption Cost Deduction. If the amount in the fund exceeds the amount necessary to reimburse the General Fund, the remaining amount would be allocated to the Department of Food and Agriculture for disbursement to eligible municipal shelters to provide food and shelter to abandoned and impounded animals.

This provision would define "Eligible municipal shelters" as a city or county animal control agency or shelter that is current on its reporting requirements to the State Department of Public Health, Veterinary Public Health Section.

IMPLEMENTATION CONSIDERATIONS

Implementing this provision would not significantly impact the department's programs and operations.

LEGISLATIVE HISTORY

AB 292 (Yamada, 2009/2010) would extend the expiration date of the Alzheimer's Disease and Related Disorders Research Fund from January 1, 2010, to January 1, 2015. This bill is currently in the Senate Revenue and Taxation Committee.

AB 1049 (Torrico, 2009/2010) would create a VCF designation on the personal income tax return for taxpayers to contribute to the Safely Surrender Babies Fund. This bill is set to be heard in the Assembly.

AB 1088 (Fletcher, 2009/2010) would create a VCF designation on the personal income tax return for taxpayers to contribute to the Morale, Welfare, and Recreation Fund for each of the veterans' homes, as provided. This bill is being held in the Assembly Veterans Affairs Committee.

SB 91 (Correa, 2009/2010) would extend the expiration date of the California Fund for Senior Citizens from January 1, 2010, to January 1, 2015. This bill is currently in the Assembly Revenue and Taxation Committee.

SB 516 (DeSaulnier, 2009/2010) would create a VCF designation on the personal income tax return for taxpayers to contribute personal funds to the California Fund for Youth. This bill is currently in the Senate Appropriations Committee.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida does not have a personal income tax but allows contribution designations on the state's motor vehicle registration and renewal forms.

None of these states provide a voluntary contribution comparable to the one proposed by this provision.

FISCAL IMPACT

This provision would not impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in the following revenue loss:

Estimated Revenue Impact of AB 233 Voluntary Contribution Effective On or After January 1, 2010 Enactment Assumed After June 30, 2009			
Pet Adoption Cost Deduction Fund	2010-11	2011-12	2012-13
	-\$15,000	-\$15,000	-\$15,000

Revenue Discussion

The revenue impact of this provision would be determined by the amount of contributions to the Pet Adoption Cost Deduction Fund and the subsequent claim of those contributions as itemized deductions in the taxable year following the contribution.

Assuming that the minimum level of contributions (\$250,000) would be achieved each year, that the fund would be reported on the 2009 return filed in 2010, and that an itemized deduction would be allowed and claimed for each contribution, potential revenue losses would be very minor.

The revenue loss would be approximately \$15,000 annually ($\$250,000 \times 6.25\%$) beginning with the taxable year the itemized deduction would be reported on the tax return (2009/2010 FY). The loss would be attributable to itemized deductions for contributions in the taxable year following the year contributions were made.

According to departmental data, the total amount of existing voluntary contributions to all funds was approximately \$4 million for 2007, with an average of \$300,000 for each designated fund.

POLICY CONCERNS

This provision would ask taxpayers to voluntarily contribute funds to offset the cost to the General Fund for allowing this tax deduction. Taxpayers who contribute funds through a voluntary contribution designation generally receive an itemized deduction for their charitable contribution.

There is a risk that the voluntary contribution proposed by these amendments would be repealed if it fails to meet the minimum contribution amount of \$250,000 in the second year that it appears on the personal income tax return. This would eliminate the reimbursement source for the Pet Adoption Cost Deduction, which would be allowed for five years, as specified.

VCF designations with contingency language are placed on the return when another VCF designation is removed from the return. It is possible that the Pet Adoption Cost Deduction Fund would not appear on the return until another designation is removed, which would delay the reimbursement to the General Fund.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 233
As Amended May 26, 2009

AMENDMENT 1

On page 8, after line 22, insert:

SEC. 4. (a) The sum of seven hundred thirty-six thousand dollars (\$736,000) is hereby appropriated to the Franchise Tax Board in augmentation of item 1730-001-0001 of the Governor's Budget, Chapter XX, Statutes of XXXX.

(b) Implementation of the deduction authorized by section 2 of this bill is contingent upon receipt of an appropriation.